

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200939002**

Release Date: 9/25/2009

Index Numbers: 355.01-00, 355.03-00

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.
Telephone Number:

Refer Reply To:

CC:CORP:B04

PLR-106555-09

Date:

June 18, 2009

LEGEND

Distributing =

Controlled =

Sub1 =

Sub2 =

Sub3 =

Business X =

Business Y =

Business Z =

Compound 1 =

Compound 2 =

Compound 3 =

Compound 4 =

Compound 5 =

Compound 6 =

Exchange =

Date1 =

Date2 =

Date3 =

a =

b =

c =

d =

e =

f =

g =

h =

i =

i =

k =

l =

m =

Dear :

This letter responds to your February 13, 2009 request for rulings on certain federal income tax consequences of a proposed transaction (the “Proposed Transaction”). The information provided in that request and in later correspondence is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding whether the Distribution (as defined below): (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code (the “Code”) and § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e) and § 1.355-7).

Summary of Facts

Distributing is the common parent of an affiliated group of corporations filing a consolidated federal income tax return (the “Distributing Group”), and wholly owns the outstanding stock of Controlled, Sub1, Sub2 and Sub3. The Distributing Group is principally engaged in Business X, Business Y and Business Z.

Distributing stock is widely held and publicly traded on the Exchange. The authorized capital stock of Distributing consists of (i) a shares of j par value voting common stock of which approximately b common shares were issued and outstanding as of Date1, and (ii) k shares of j par value preferred stock, of which c shares were issued and outstanding. As of Date1, Distributing had d shareholders who owned five percent or more of the common stock of Distributing. Distributing has a Stockholder Rights Plan which allows common stockholders to exercise a right to purchase units of preferred stock upon certain triggering events.

Distributing maintains a stock option plan for certain employees and directors. As of Date1, options to acquire e shares of Distributing common stock were

outstanding. The price of the option reflects the fair market value of the underlying Distributing common stock on the date of grant. Distributing also has an Employee Stock Purchase Plan under which a maximum of f shares of common stock may be purchased by eligible employees. As of Date1, g shares of common stock had been purchased under this plan. None of these plans give the shareholders a right to vote, proceeds upon liquidation or dividends if declared.

Prior to the proposed transaction, Distributing is engaged in Business X, Sub1 is engaged in Business Y and Sub2 is engaged in Business Z. Sub 3 is an inactive entity and is not relevant to the proposed transaction.

Financial information has been submitted indicating that the Business X business (as conducted by Distributing) and the Business Y business (as conducted through Sub1) had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Distributing Group's management has determined that separating Business Y from Business X and from portions of Business Z will serve a number of corporate business purposes.

Proposed Transaction

To separate Business Y from Business X and from portions of Business Z, taxpayer proposes the following series of transactions (the "Proposed Transaction"):

- (i) On Date3, Distributing formed Controlled.
- (ii) The following Sub2 assets related to the Business Z business will either be distributed to Distributing and subsequently contributed to Controlled as described in Step (iii) below, or sold directly to Controlled ("Acquired Sub2 Assets"): (i) FDA regulatory documentation related to Compound 1, Compound 2, Compound 4, and Compound 6, and certain preclinical compounds and target research (and related proprietary technology), and (ii) the fixed assets and employees associated with Business Z. Sub2 will retain the FDA regulatory documentation with respect to two compounds, Compound 3 and Compound 5. Sub2 intends to seek third party collaboration or licensing agreements for the further development of these compounds for which Sub2 anticipates it will receive licensing fees, with an upfront payment and then additional payments if certain milestones are achieved.
- (iii) Distributing will contribute the following assets to Controlled (the "Contribution"): (i) Business X, including employees, contracts, all rights to processes, protocols and related intellectual property rights associated with Business X; (ii) h-i of cash (to be determined by Distributing); (iii) rights to

intellectual property or proprietary information held by Distributing but used by Sub2 in Business Z; and (iv) the Sub2 Acquired Assets if distributed to Distributing in Step (ii) above.

- (iv) Immediately prior to the Distribution, Controlled will amend its capital structure to authorize l shares of j par value voting common stock, of which approximately m shares will be issued and outstanding, and (ii) k shares of j par value preferred stock, of which no shares will be issued and outstanding. Controlled will also adopt the following plans, which will be similar to the plans that Distributing has: (i) a stockholders rights plan, (ii) an employee stock purchase plan, and (iii) an employee stock option plan.
- (v) On Date2, Distributing will distribute all of the stock of Controlled pro-rata to its shareholders (the "Distribution"). For every four shares of Distributing stock a shareholder will receive one share of Controlled stock. Holders of stock options in Distributing will receive stock options in Controlled in the same four shares for one ratio. No fractional shares of Controlled will be issued.
- (vi) Distributing and Controlled will also enter into a sub-lease agreement for the leasing of certain separated facilities for use by Controlled. It is anticipated that the lease payments will be a pass through of the lease costs to Distributing under its master lease for the premises. In addition, Distributing and Controlled will enter into a Separation and Distribution Agreement, Tax Sharing Agreement and an Employee Matters Agreement, under which Controlled assumes responsibility for post Distribution costs and responsibilities for the employees transferred to Controlled.

Representations

The following representations are made regarding the Contribution and Distribution:

- (a) The indebtedness, if any, owed by Controlled to Distributing immediately after the Distribution will not constitute stock or securities.
- (b) No part of the consideration to be distributed by Distributing to its shareholders will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.
- (c) Business X conducted by Distributing nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part.

(d) Business Y conducted by Sub1 nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part.

(e) Distributing and Sub1 are, and immediately after the Distribution will be, members of Distributing's separate affiliated group (within the meaning of 355(b)(3)(B)) (the "Distributing SAG").

(f) Sub1, immediately after the Distribution, will be affiliated with Distributing in a manner that satisfies the ownership test of § 1504(a), without regard to § 1504(b).

(g) The five years of financial information submitted on behalf of the Business X business directly conducted by Distributing is representative of its present operations, and with regard to such operations, there have been no substantial operational changes since the date of the last financial statements submitted.

(h) The five years of financial information submitted on behalf of the Business Y business conducted by Sub1 is representative of its present operations, and with regard to such operations, there have been no substantial operational changes since the date of the last financial statements submitted.

(i) Following the Distribution, Controlled and Sub1 will each continue, independently and with its separate employees, the active conduct of its business conducted by Distributing or Sub1 prior to the Proposed Transaction.

(j) The Distribution will be carried out for the following corporate business purposes: (i) enable Distributing and Controlled to focus on and maximize core technology strengths relative to their individual businesses; (ii) alleviate competition between the businesses for allocation of internal resources, including laboratory space and equipment, capital spending and capital allocations, and intellectual resources; (iii) allow each business to more effectively plan and pursue long-term strategic initiatives; (iv) allow each business to compete more effectively in each business's respective markets; and (v) improve the intrinsic value of each separate business to facilitate financial flexibility. The distribution of the stock of Controlled is motivated, in whole or substantial part, by these corporate business purposes.

(k) The Distribution is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.

(l) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50% or more of the total value of shares of all classes of Distributing stock, that was acquired

by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(m) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50% or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(n) The Distribution is not part of a plan or series of related transactions (within the meaning of Treas. Reg. § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50% or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

(o) The total adjusted basis and total fair market value of the assets transferred to Controlled by Distributing will exceed the sum of the total liabilities assumed, if any, (within the meaning of § 357(d)) by Controlled and will exceed the amount, if any, of liabilities owed to Controlled by Distributing that are discharged or extinguished in connection with the exchange. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.

(p) The liabilities, if any, assumed (within the meaning of § 357(d)) by Controlled and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.

(q) Except for indebtedness that may be created in the ordinary course of business or in connection with the Sublease Agreement, Employee Matters Agreement, Separation and Distribution Agreement or Tax Sharing Agreement, no indebtedness will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.

(r) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (see §§ 1.1502-13 and 1.1502-14 in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Distributing will not have an excess loss account in the stock of Controlled.

(s) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(t) Neither Distributing nor Controlled is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).

(u) Immediately after the Distribution (taking into account § 355(g)(4)), (i) neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)), and (ii) no person will hold a 50% or more interest (within the meaning of § 355(g)(3)) in the stock of Distributing or Controlled that such person did not hold immediately before the Distribution.

(v) Distributing, Controlled, and the Distributing shareholders will each pay their own expenses, if any, incurred in connection with the Contribution and Distribution.

(w) Any payment of cash in lieu of fractional shares of Controlled stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing and maintaining fractional shares and will not represent separately bargained for consideration. It is intended that the total cash paid in the Distribution to shareholders in lieu of fractional shares of Controlled stock will not exceed one percent of the total consideration that will be distributed in the Distribution. The fractional share interests of each Distributing shareholder will be aggregated, and it is intended that no shareholder will receive cash in an amount equal to or greater than the value of one share of Controlled stock.

Rulings

Based solely on the information submitted and representations set forth above, we rule as follows:

(1) The Contribution, followed by the Distribution, will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled will each be “a party to a reorganization” under § 368(b).

(2) No gain or loss will be recognized by Distributing on the Contribution (§ 357(a) and 361(a)).

(3) No gain or loss will be recognized by Controlled on the Contribution (§ 1032(a)).

(4) The basis of each asset received by Controlled in the Contribution will equal the basis of that asset in the hands of Distributing immediately before its transfer (§ 362(b)).

(5) The holding period of each asset received by Controlled in the Contribution will include the period during which that asset was held by Distributing (§ 1223(2)).

(6) No gain or loss will be recognized by (and no amount will be included in the income of) the shareholders of Distributing on the Distribution of the Controlled stock (§ 355(a)(1)).

(7) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)(1)).

(8) The aggregate basis of the Distributing stock and Controlled stock in the hands of the shareholders of Distributing after the Distribution will be the same as the basis of the Distributing stock in the hands of the shareholders of Distributing immediately before the Distribution (§§ 358(a) and 1.358-1(a)). Such basis will be allocated between the Distributing stock and the Controlled stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§§ 358(b)(2) and 358(c)).

(9) The holding period of the Controlled stock received by the shareholders of Distributing in the Distribution will include the holding period of the Distributing stock with respect to which the Distribution will be made, provided that such Distributing stock is held as a capital asset by the shareholders of Distributing on the date of the Distribution (§ 1223(1)).

(10) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under §§ 1.312-10(a) and 1.1502-33(e)(3).

(11) A shareholder who receives cash in lieu of fractional shares of Controlled stock will recognize gain or loss measured by the difference between the basis of the fractional share received, as determined above, and the amount of cash received (§ 1001). Any gain or loss will be treated as capital gain or loss, provided the fractional share of stock would be held as a capital asset on the date of the Distribution (§§ 1221 and 1222).

Caveats

No opinion is expressed about the tax treatment of the Proposed Transaction under other provisions of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Proposed Transaction that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding whether the Distribution: (i) satisfies the business purpose requirement of § 1.355-2(b), (ii) is used principally as a device for the distribution of the earnings and profits of the Distributing corporation or the Controlled corporation or both (see § 355(a)(1)(B) and § 1.355-2(d)), (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the Distributing corporation or the Controlled corporation (see § 355(e) and § 1.355-7). In addition, no opinion is expressed regarding the federal income tax consequences of the transfer by Sub2 of the Acquired Sub2 Assets to Distributing or to Controlled that is not part of the Contribution.

Procedural Statements

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

In accordance with the power of attorney on file in this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Richard K. Passales
Senior Counsel, Branch 4
Associate Chief Counsel (Corporate)

cc: